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SUBJECT: PRICE CONTROLS AS A MEASURE TO STOP FOOD INFLATION

REFTEL: A) Quito 557, B) 07 Quito 2095, C) Quito 36, D) 07 Quito 2114,

¶1. (SBU) Summary: The Correa administration imposed mandatory price controls on nine products on August 28, although it said that all the controls are based on agreements with producers. The GOE continues to intervene in the market to limit food price inflation, but has shown some flexibility in its interventions. End Summary.

Expanded Price Controls

¶2. (U) On August 28, the GOE established price controls on nine products: noodles, vegetable oil, wheat, sugar, canned tuna, chicken parts, rice, milk and bread (the last three products were already subject to varying forms of price controls). According to Susana Cabeza de Vaca, Coordinating Minister of Production, the price controls are based on agreements between the government and the private sector.

¶3. (U) The extent, rigidity, and duration of the price controls vary by product. Some of the products have already been subject to price controls, notably milk. Some products are subject to price controls until mid-October, others until the end of the year. The price control on bread only applies to "pan popular," small buns that cost 10 cents. The highest quality milk is exempt from price controls. The price control on chicken parts is not a fixed amount; instead, producers have agreed prices will not rise above their levels in July. Price controls for tuna are "variable," which presumably allows different qualities to be priced separately.

¶4. (U) Media reporting shortly after the price controls were unveiled showed mixed compliance with the controls. According to one report, prices in large supermarkets were in some instances less than the price ceilings, while prices in small corner grocery stores often exceeded the limits.

Experimenting with Controls as Inflation Rises
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¶5. (SBU) Inflationary pressures began to rise in the second half of 2007, although the annual rate for the year was only 3.3% due to low inflation in the first half of the year. Prices increased rapidly in 2008, with an annual rate of 10.02% in August. The inflation is due in large measure to increasing international prices for food and petroleum derivatives (fuel prices are frozen in Ecuador), but also to domestic pressures from natural disasters (flooding, volcanic eruptions) and increased demand due to increased government spending and transfers.

¶6. (U) Starting in mid-2007, the GOE has pursued a mixed bag of market-intervention measures to fight inflation. These include tax breaks and subsidies for farmers (ref a), a ban on rice exports (ref. b), milk price controls (ref. c), and subsidies for flour used in bread (ref d).

¶7. (SBU) As it has extended market interventions, the GOE has experimented. For example, it first imposed milk price controls with little consultation with the dairy industry. In renewing the controls, it consulted with the industry and as a result marginally increased the ceilings and exempted the highest-end product, ultapasteurized milk in boxes, from controls. After food prices began accelerating in the second quarter of 2008, the GOE tried a package of tax incentives and subsidies for farmers, rather than expanding the scope of price controls. As bread prices increased, the GOE first offered subsidized flour to maintain prices, then tried voluntary price controls on "pan popular," and finally imposed firm price controls on the inexpensive bread. However, it has left prices for other types of bread uncontrolled.

Comment

¶8. Inflation is a political vulnerability for the GOE. In attempting to limit inflation, it has responded with a mix of market intervention measures. However, it also seems to realize the limited effectiveness of price controls and their potential to suppress supplies, so has been experimenting on how to proceed. Looking forward, it is not clear whether the GOE will limit market interventions to occasional, flexible controls or will impose broader, tighter controls.

HODGES